
NO. 12084

IN THE

United States
Circuit Court of Appeals
FOR THE NINTH CIRCUIT

S. P. BEECHER, Farm Debtor-
Bankrupt, *Appellant*

vs.

UNITED STATES OF AMERICA,
Claimant-Appellee

Upon Appeal from the District Court of the United
States, for the Eastern District of Washington

HONORABLE SAM M. DRIVER, *Judge*

BRIEF FOR THE CLAIMANT-APPELLEE

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JURISDICTION

This appeal involves a judgment of the District Court allowing the claim of the United States as a valid and subsisting lien for income taxes assessed against the farm debtor appellant for the fiscal year ended February 28, 1942, as a valid and subsisting lien against a fund in possession of the Leavenworth Fruit and Cold Storage Company, authorizing and directing said company to pay said fund to the Collector of Internal Revenue for and on behalf of the United States (R. 1168-1170).

QUESTION PRESENTED

Whether the District Court erred in allowing the claim of the United States as a valid and subsisting lien and ordering said lien claim paid out of a fund in possession of the Leavenworth Fruit and Cold Storage Company.

STATUTES AND OTHER AUTHORITIES
INVOLVED

The statute and other authorities are set out in the Appendix, *infra*.

STATEMENT

The facts presenting succinctly the question involved may be summarized as follows:

The farm debtor appellant, hereinafter referred to as the taxpayer, on July 31, 1939, filed a petition in bankruptcy under Sec. 75 of the Bankruptcy Act, and on the same date the petition was approved and an order of reference entered (Tr. 10391, pp. 9-14).

No acceptable plan was presented to the Conciliation Commissioner, and on February 1, 1940, the taxpayer was adjudicated bankrupt under Sec. 75 (s) of the Bankruptcy Act, and an order of general reference was entered (Tr. 10391, pp. 57-58).

The taxpayer continued in possession of all of his property and continued to operate the same under the rental order and order staying proceedings as

entered by the Conciliation Commissioner on April 30, 1940, and as modified by the District Court by order of November 2, 1940 (Tr. 10391, pp. 91-96 and 162-164).

On August 17, 1943, Harold D. Couch was duly appointed and qualified as Receiver of the bankrupt estate (R. 221).

On or about August 27, 1943, the taxpayer filed his delinquent individual income tax return for the fiscal year stated beginning March 1, 1941, and ending March 1, 1942, and disclosing a net income of \$589.60, and no tax due. No income was shown from his operation as debtor in possession or trustee of his farm properties (R. 133-A, Government's Exhibit 2).

On or about October 27, 1944, the taxpayer and the Receiver were advised that a determination of the taxpayer's income tax liability for that period disclosed additional net farm income from operations in the amount of \$4,639.16, and a deficiency in tax of \$530.92 and \$132.73 in penalty. A statement of the adjustments to net income, explanation of adjustments, and computation of tax were attached (R. 135-137, Government's Exhibit 3).

Pursuant to the provisions of Sec. 274 of the Internal Revenue Code (Title 26, U.S.C. Sec. 274), the Commissioner of Internal Revenue on November 10, 1944, duly assessed the aforementioned tax and penalty (R. 133, Government's Exhibit 1).

On November 13, 1944, and December 8, 1944, the Collector of Internal Revenue for the District of Washington, on behalf of the United States, filed with the Clerk of the District Court and with the Receiver a duly verified proof of claim and corrected proof of claim for the tax and penalty assessed (R. 128-132).

The Receiver, after receiving notice of the deficiency assessment, notified the taxpayer of his right of protest, and receiving no word from him, filed through his attorney a protest with the Treasury Department, which protest, after hearing, was denied. Thereafter, on or about April 4, 1945, the Receiver filed a petition with the District Court for direction with respect to the payment of the Government's claim from funds in the hands of the Receiver or from the funds impounded by the Court and then in possession of the Leavenworth Fruit and Cold Storage Company. At the hearing on May 23, 1945, an order was entered directing that action on the claim of the United States be deferred to a later date to be fixed by the Court in order to allow the taxpayer to be further heard (R. 227).

On March 11, 1946, and prior to that date when the mandate in Cause No. 10391 was entered, the Collector of Internal Revenue caused to be filed a notice of lien and served upon the Leavenworth Fruit and Cold Storage Company a levy for distraint covering the taxes and penalties assessed, as aforesaid, and at which time the Leavenworth Fruit and Cold

Storage Company was indebted to the taxpayer in the amount of \$3,412.07 from the proceeds from his operation as debtor in possession (R. 1169).

On April 30, 1946, and pursuant to the mandate of this Court, an order was entered directing the Conciliation Commissioner to enter an order that possession under the supervision and control of the Court of all of the taxpayer's property remain in the taxpayer subject to all existing liens and encumbrances, except that any order made by the Conciliation Commissioner granting to the taxpayer the right of possession was to exclude the \$800.00 of the funds then in the possession of the Leavenworth Fruit and Cold Storage Company for the protection of the lien of the United States (R. 13-15). This Court affirmed the order as a proper protection for the Government's tax lien (160 F. (2d) 294).

On March 24, 1947, the taxpayer filed a motion to vacate and set aside the levy and distraint by the United States filed with the Leavenworth Fruit and Cold Storage Company (R. 30-32).

Pursuant to notice mailed to the taxpayer on April 22, 1947, hearing on the claim of the United States as well as on the motion of the taxpayer for release of the funds was had before the Court on May 7, 1947. The taxpayer moved for continuance of the hearing on the merits of the claim but not as to his motion.

The hearing was held on May 7, 1947, at which

time evidence was taken and exhibits introduced subject to the taxpayer's objections and further hearing if deemed advisable (R. 39-40, 48).

Pursuant to an order of June 3, 1947, re-hearing on the taxpayer's motion to release attachment was held on December 11, 1947 (R. 523-525), taxpayer and his estate being represented by Attorney Earle E. Horswill, pursuant to the order of appointment (R. 891).

No specific exceptions or objections were or have been filed to the allowance of the Government's claim.

The deficiency assessment was based upon the gross receipts from the sale of fruit of \$14,669.32 received by the taxpayer from his operations of the farm properties in the fiscal year involved and admittedly not reflected in his income tax return filed for the fiscal year stated to be ended March 1, 1942, which return was entirely erroneous, as admitted by the taxpayer (R. 78-82, 86).

The restraining order complained of was not entered until April 12, 1943, and affected receipts accrued and received subsequent to the tax year involved (Tr. 10391, pp. 57).

Taxpayer offered no evidence to refute the Commissioner's determination, and his principal contention was, and has been, that he was not liable for taxes on the income from his operations after his adjudication (R. 80-81).

SUMMARY OF ARGUMENT

The taxpayer, in possession of and operating the estate prior to his rent-paying tenancy under the farmer-debtor provisions of the Bankruptcy Act, being that of a trustee for creditors under the supervision of the Bankruptcy Court, was required to file a return and pay taxes due on the net income received.

The claim filed by the Collector, even though objected to, constitutes *prima facie* evidence of the facts sworn to therein, and the assessment constitutes *prima facie* evidence in support of the claim.

The taxpayer has failed to assume his burden of proving that he did not owe the tax liability assessed, which was allowed and ordered paid out of the fund set aside and held for that purpose.

The taxpayer was given repeated hearings and opportunities to present evidence and offer any valid objections that he might have to the allowance and payment of the claim, and, therefore, none being offered, the order appealed from was properly entered.

ARGUMENT

I.

The taxpayer was liable for a return and the payment of the tax.

It is without dispute that the taxpayer after his adjudication was in possession of all of his property, operated the same, and received all of the income therefrom during the period involved, or prior to his rent-paying tenancy.

Admittedly, the taxpayer received \$14,669.32 gross receipts from the sale of fruits from his property, and the Commissioner of Internal Revenue allowed deductible expenses of \$10,030.16, leaving a net taxable income from the sale of fruit of \$4,639.16, which was entirely omitted from his return (Government's Exhibits 2 and 3; R. 133a, 140).

It is clear that under the taxing statute and regulations, he was liable for a return and payment of the tax due on such income (Secs. 51 (a) (e) and 142 (a) (3) of the Internal Revenue Code, and Sec. 19.142-4, Regulations 103, *infra*).

The taxpayer's primary argument seems to be that he had no taxable income because his affairs were and still are being administered under the farmer-debtor provisions of the Bankruptcy Act, and that as such, his estate was undetermined and is still in litigation. His argument does not admit of the mandatory provisions of the taxing acts that a debtor in

possession of his property and receiving income therefrom is liable for a return and payment of the tax due thereon.

Admittedly, the taxpayer received during the taxable year ended February 28, 1942, gross income of \$14,669.32 in addition to the amount shown on his return of \$598.60. His only showing of failure to receive such income or any restricted use thereof is his reference to the restraining order of April 12, 1943. This order, however, was not issued until more than a year after the close of the taxable year involved.

This order specifically restrained and enjoined the Leavenworth Fruit and Cold Storage Company from paying to the taxpayer any of the money then in its possession "as proceeds of the 1942 fruit crop." It is the "proceeds of the 1941 fruit crop" of \$14,669.32 which were received and used by the taxpayer, and which gave rise to the tax involved. Prior to the restraining order, the taxpayer not only received all of the proceeds from his prior years' operations, but failed to file with the court any report for his receipts and expenditures for those years (Tr. 10391, Vol. 11, p. 366).

It is clear from the record that the taxpayer had unrestricted and free use to the proceeds from the sale of his 1941 crop in the sum of \$14,669.32, which gave rise to the additional assessment here involved.

None of the cases relied upon by the taxpayer supports his theory that a debtor in possession of his

property and operating the same under the farmer-debtor provisions of the Bankruptcy Act is not liable for the tax. His operation of his property under the supervision of the court does not of itself deny the receipt of the income nor that his estate was correspondingly increased in value by such income.

Taxpayer cites and relies upon *H. Lieber & Co. v. Commissioner of Internal Revenue*, 90 F. (2d) 932. That case involved a question of when income accrued on the proceeds of a money judgment. Such a question is foreign to any issue here involved, and the case, if anything, sustains the lower court's order on the ground that a taxpayer objecting to a deficiency assessment has the burden of overcoming the presumption of the correctness of the Commissioner's determination.

All of the other cases cited by the taxpayer are neither in point factually, nor involve questions pertinent to the points raised on appeal. We therefore hesitate to further encumber this brief with additional references thereto.

II.

The Government's claim filed with the Receiver was in proper form and was duly allowed as a lien claim against the fund which was held for this purpose.

The undisputed facts show that the taxpayer neglected to file a proper return, and a notice of a

proposed deficiency was mailed to him and his Receiver. The deficiency assessment was duly made under the provisions of the Bankruptcy Act, and the tax not being paid upon demand, a proof of claim and a corrected proof of claim were properly filed with the Receiver and with the Clerk of the United States District Court.

Prior to the date when the order on mandate was entered, the Collector filed a notice of lien and served a levy against the funds of the taxpayer in possession of the Leavenworth Fruit and Cold Storage Company. The District Court, in its order on the mandate, requested \$800.00 of these funds, and this Court, in affirming that order on appeal, stated, "We think the order was a proper protection of the Government's tax lien." (160 F. (2d) 294).

The taxpayer contends that he had no notice in detail as to how the deficiency was computed, so that he could furnish evidence as to why the deficiency was incorrect.

We submit that such a contention, like most of his other contentions, can hardly be reconciled with the record in this case. It is undisputed that the taxpayer was given notice of the proposed deficiency, with detailed statement attached; he was given notice of his right to file a protest from such proposed deficiency, and making none, a protest was filed by the Receiver on his behalf, which protest after hearing was denied on its merits. The hearing on the Government's claim was first set before the District

Court on the Receiver's report, and thereafter continued to give the taxpayer an opportunity to be heard. A subsequent hearing, after due notice, was again held on May 7, 1947, and a further re-hearing on December 11, 1947, after due notice to the taxpayer. In the latter hearing the taxpayer appeared in person and was represented in court by Earle W. Horswill, his attorney.

So far as the record shows, we know of no case in which a taxpayer has been given so many opportunities to file exceptions or make valid objections to the allowance of the Government's claim in bankruptcy.

No objections or exceptions to the allowance of the claim have ever been filed except the taxpayer's motion to release the attachment and distraint. This motion, of course, is a restatement of the taxpayer's objection to the order on mandate, and the question raised by the motion is moot, or if not, *res judicata*, by the affirmance of the order.

It has long been the rule that claims filed by the United States in bankruptcy proceedings, even though objected to, constitute *prima facie* evidence of the facts sworn to therein, (1) for the reason that in *Whitney v. Dresser*, 200 U. S. 532 (1906), the Supreme Court held that the implications of the Act and considerations of practical convenience and just administration required such effect, and (2) in the case of tax claims based upon assessments by the Commissioner of Internal Revenue, for the additional reason that

the assessment constitutes *prima facie* evidence in support of the claim. *United States v. Rindskopf*, 105 U.S. 418.

III.

The points relied upon by the taxpayer on appeal are neither supported by the record or the law in the case.

(1) We have heretofore pointed out that the taxpayer utterly failed to show that he did not receive the taxable income from the sale of his 1941 fruit crop, nor that he did not have free and unrestricted use of those funds. The restraining order was effective only in restraining funds of a later year and has no application to the income for the year involved.

(2) The procedure followed by the Government was in strict compliance with the statute and regulations relative to bankruptcy proceedings, as was heretofore held by this Court on the taxpayer's appeal from the order on mandate.

(3) The record clearly shows that the taxpayer was never denied a hearing on the merits of the claim, but was granted repeated hearings and continuances over a period of several years. The lower court, in this respect, was more than lenient in allowing the taxpayer numerous opportunities to be heard.

(4) The order appealed from was a proper order allowing the claim as filed, as there were no valid

exceptions or objections filed and no competent evidence introduced or submitted, nor any issue of fact formed which warranted any further findings than those set forth in the judgment order.

(5) Contrary to plaintiff's contention, proper verified proofs of claim were duly filed in the proceeding.

(6) The jurisdiction of the District Court can hardly be questioned, since this Court, in its affirmance of the order on mandate, expressly approved the withholding of the funds in possession of the Leavenworth Fruit and Cold Storage Company for the payment of the amount of the Government's tax lien determined to be due.

We respectfully submit that the District Court did not err, and the judgment order appealed from should be affirmed.

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APPENDIX

Internal Revenue Code:

Sec. 274. *Bankruptcy and Receiverships.*

(a) *Immediate assessment.*—Upon the adjudication of bankruptcy of any taxpayer in any bankruptcy proceeding or the appointment of a receiver for any taxpayer in any receivership proceeding before any court of the United States or of any State or Territory or of the District of Columbia, any deficiency (together with all interest, additional amounts, or additions to the tax provided for by law) determined by the Commissioner in respect of a tax imposed by this chapter upon such taxpayer shall, despite the restrictions imposed by section 272 (a) upon assessments be immediately assessed if such deficiency has not heretofore been assessed in accordance with law. * * * (26 U.S.C. 1940 ed., Sec. 274).

Treasury Regulations 103:

Sec. 19.274-1. *Bankruptcy and receivership proceedings.*—During a bankruptcy proceeding, or an equity receivership proceeding in either a Federal or a State court, the assets of the taxpayer are in general under the control of the court in which such proceeding is pending, and the collection of taxes cannot be made by distraining upon such assets. However, any assets which under applicable provisions of law are not under the control of the court may be subject to distraint.

As used in these regulations the term “bankruptcy proceeding” includes proceedings under * * * section * * * 75, * * *; and the term “adjudication of bankruptcy” includes, * * * the filing of a petition under section * * * or 75 * * * with a court of competent jurisdiction.

A trustee in bankruptcy (including a trustee, receiver, debtor in possession, or other person designated as in control of the assets of a debtor in any bankruptcy proceeding by order of the court in which such proceeding is pending) or a receiver in any receivership proceeding is required to give notice in writing to the Commissioner of Internal Revenue in Washington, D.C., of the adjudication of bankruptcy or the appointment of a receiver.

Internal Revenue Code:

Sec. 51. *Individual Returns.*

(a) *Requirement.*—The following individuals shall each make under oath a return stating specifically the items of his gross income and the deductions and credits allowed under this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe—

* * *

(e) *Fiduciaries.*—For returns to be made by fiduciaries, see section 142. (26 U.S.C. 1940 ed., Sec. 51)

Sec. 142. *Fiduciary Returns.*

(a) *Requirement of return.*—Every fiduciary (except a receiver appointed by authority of law in possession of part only of the property of an individual) shall make under oath a return for any of the following individuals, estates, or trusts for which he acts, stating specifically the items of gross income thereof and the deductions and credits allowed under this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe—

(1) Every individual having a net income for the taxable year of \$1,000 or over, if single, or if married and not living with husband or wife;

* * *

(26 U.S.C. 1940 ed., Sec. 142)

Treasury Regulations 103:

Sec. 19.142-1. *Fiduciary returns*.—Every fiduciary, or at least one of joint fiduciaries, must make a return of income—

(a) For the individual whose income is in his charge, if the gross income of such individual is \$5,000 or over, or if the net income of such individual is \$1,000 or over if single or if married and not living with husband or wife for any part of the taxable year; or if such individual is married and was living with husband or wife for any part of the taxable year but not at the close of the taxable year and his gross income for the taxable year is \$5,000 or over, or his net income is equal to, or in excess of, the credit allowed him by section 25 (b) (1) and (3) (computed without regard to his status as head of a family); or if such individual is married and was living with husband or wife for the entire taxable year and the aggregate gross income of both husband and wife is \$5,000 or over, or the aggregate net income of both husband and wife is \$2,500 or over; or if such individual is married and was living with husband or wife at the close of the taxable year but not during the entire taxable year and the aggregate gross income of both husband and wife is \$5,000 or over, or the aggregate net income of both husband and wife is equal to, or in excess of, the credit allowed them by section 25 (b) (1) and (3) (computed without regard to the status of either of them as head of a family), or

* * *

The return in case (a) shall be on Form 1040 or 1040 A. * * *

Sec. 19.142-4. *Return by receiver.*—A receiver who stands in the stead of an individual or corporation must render a return of income and pay the tax for his trust, but a receiver of only part of the property of an individual or corporation need not. If the receiver acts for an individual the return shall be on Form 1040 or 1040 A. * * * In general, statutory receivers and common law receivers of all the property or business of an individual or corporation must make returns.